

A REPORT
TO THE
ARIZONA LEGISLATURE

Accounting Services Division

Compliance Review

Continental Elementary School District No. 39

Year Ended June 30, 2007



Debra K. Davenport
Auditor General

The **Auditor General** is appointed by the Joint Legislative Audit Committee, a bipartisan committee composed of five senators and five representatives. Her mission is to provide independent and impartial information and specific recommendations to improve the operations of state and local government entities. To this end, she provides financial audits and accounting services to the State and political subdivisions, investigates possible misuse of public monies, and conducts performance audits of school districts, state agencies, and the programs they administer.

Accounting Services Division Staff

Gregory Rickert, Manager and Contact Person
grickert@azauditor.gov

Elizabeth Ullman
Lisa Ashton

Copies of the Auditor General's reports are free.
You may request them by contacting us at:

Office of the Auditor General
2910 N. 44th Street, Suite 410 • Phoenix, AZ 85018 • (602) 553-0333

Additionally, many of our reports can be found in electronic format at:

www.azauditor.gov



DEBRA K. DAVENPORT, CPA
AUDITOR GENERAL

STATE OF ARIZONA
OFFICE OF THE
AUDITOR GENERAL

WILLIAM THOMSON
DEPUTY AUDITOR GENERAL

January 27, 2009

Governing Board
Continental Elementary School District No. 39
P.O. Box 547
Green Valley, AZ 85622-0547

Members of the Board:

We have reviewed the District's audit reports and Uniform System of Financial Records (USFR) Compliance Questionnaire for the year ended June 30, 2007, prepared by Heinfeld, Meech & Co., P.C., to determine whether the District substantially complied with the USFR.

As a result of our review, we noted significant deficiencies in internal controls that indicate the District had not complied with the USFR. District management should implement the recommendations we have described in this report within 90 days after the date of this letter. We have communicated specific details for all deficiencies to management for correction.

We also noted that the auditors qualified their opinion on the District's financial statements for the year ended June 30, 2007, because the District did not maintain adequate capital asset records.

During the 90-day period, the District may request a meeting to discuss these recommendations with my Office and the Arizona Department of Education by calling Magdalene Haggerty, Accounting Services Director, or Gregg Rickert, Accounting Services Manager.

A member of my staff will call the Business Manager in several weeks to discuss the District's action to implement these recommendations. After the 90-day period, my staff will schedule an on-site review of the District's internal controls to determine whether the District is in substantial compliance with the USFR. Our review will cover the deficiencies we have communicated to management, as well as any other internal control deficiencies we are aware of at the time of our review.

Sincerely,

Debra K. Davenport
Auditor General

TABLE OF CONTENTS



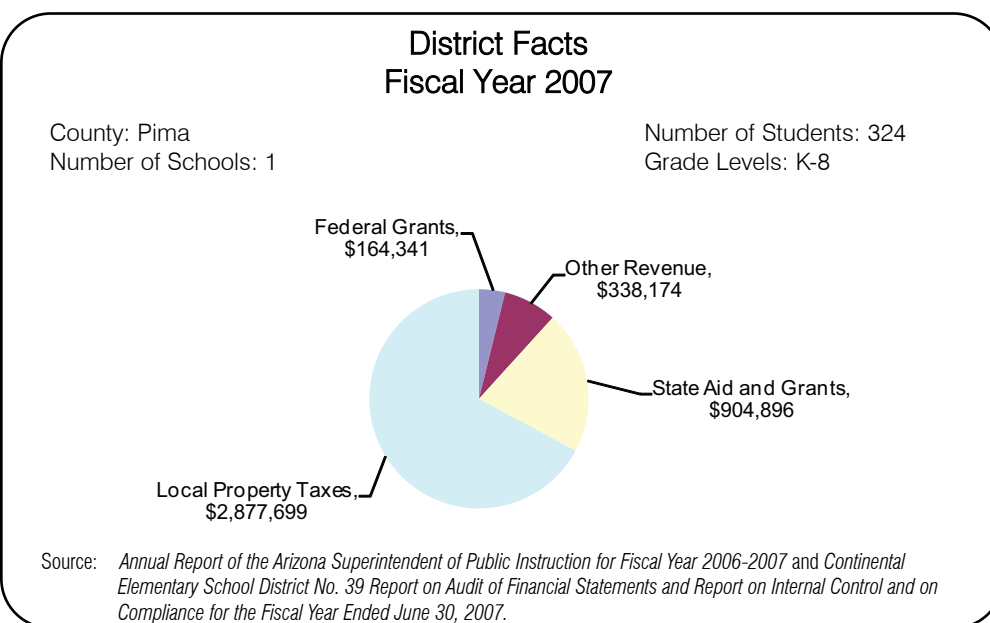
Introduction	1
Finding 1: The District's controls over competitive purchasing and expenditures should be strengthened	2
Finding 2: The District should improve its controls over capital assets	4
Finding 3: The District should ensure the accuracy of its accounting records and improve its financial reporting	6
Finding 4: The District's controls over its bank accounts and cash should be strengthened	8

INTRODUCTION

Continental Elementary School District No. 39 is accountable to its students, their parents, and the local community for the quality of education provided. The District is also financially accountable to taxpayers for over \$4.2 million it received in fiscal year (FY) 2007 to provide this education.

The District should use effective internal controls to demonstrate responsible stewardship for the tax dollars it receives. These controls are set forth in the *Uniform System of Financial Records* (USFR), a joint publication of the Office of the Auditor General and the Arizona Department of Education (ADE). The policies and procedures in the USFR incorporate finance-related state and federal laws and regulations and generally accepted accounting principles applicable to school districts. Districts are legally obligated to comply with USFR requirements, and doing so is good business practice.

As a result of our review of the District's audit reports and USFR Compliance Questionnaire for the year ended June 30, 2007, we determined that the District had failed to comply with the USFR. In addition, because of inadequate capital asset records, the District's auditors qualified their opinion on the District's financial statements for the year ended June 30, 2007. We noted certain deficiencies in controls that the District's management should correct to ensure that it fulfills its responsibility to establish and maintain adequate financial stewardship and to comply with the USFR. Our recommendations are described on the following pages.



FINDING 1

The District's controls over competitive purchasing and expenditures should be strengthened

The District may not have received the best value for the public monies it spent.

School District Procurement Rules for competitive sealed bidding and USFR guidelines for purchases below the competitive sealed bid threshold promote open and fair competition among vendors. This helps ensure that districts receive the best possible value for the public monies they spend, and that its expenditures are appropriate, approved, and adequately supported. However, the District did not always follow the School District Procurement Rules or the USFR guidelines. For example, the District did not always issue invitations for bids or requests for proposals for purchases that exceeded the competitive sealed bid threshold. Also, the District did not always maintain documentation that due-diligence procedures were performed for a sample of purchases made through a purchasing cooperative. Additionally, the District did not always obtain oral and written price quotations for purchases that required them.

Further, the District's expenditures were not always within the authorized purchase order amount and the District exceeded its Maintenance and Operation Fund budget as of June 30, 2007. In addition, the District's Governing Board adopted credit card policy did not include dollar limits for charges, and the District did not prepare a fiscal year 2007 list of liabilities or file an Advice of Encumbrance with the County School Superintendent (CSS).

Recommendations

To strengthen controls over competitive purchasing and expenditures, the District should:

- Issue invitation for bids or requests for proposals for purchases of construction, materials, or services that exceed \$33,689.
- Review documentation from each purchasing cooperative for at least a sample of the contracts the District wishes to use, and document the due-diligence procedures performed.
- Obtain oral price quotations from at least three vendors for purchases estimated to cost between \$5,000 and \$15,000, and written quotations from at least three vendors for purchases estimated to cost between \$15,000 and \$33,689. If the District cannot obtain three price quotations, it should document the vendors contacted who did not offer price quotations and their reasons for not providing quotations.

School District Procurement Rules provide the requirements for:

- Competitive sealed bids for goods and services in excess of \$33,689.
- Competitive sealed proposals for goods and services when factors other than the lowest cost are appropriate.

- Ensure that purchases do not exceed the approved purchase order amounts. If the District wishes to make purchases in excess of approved purchase orders, the existing purchase order should be revised and re-approved or a new purchase order should be prepared.
- Verify that sufficient budget capacity is available in budget-controlled funds before authorizing expenditures from them.
- Maintain formal, written policies governing the use of credit cards that include dollar limits for charges.
- Prepare an Advice of Encumbrance for liabilities payable as of June 30 for all levy funds and file with the CSS on or before July 18.

FINDING 2

The District should improve its controls over capital assets

The District's auditors issued a qualified opinion on the financial statements because the District did not maintain adequate capital assets records.

The District has invested a significant amount of money in its capital assets and stewardship items. In order to protect its investment, the District should have complete and accurate lists of these assets to ensure they are properly identified, accounted for, and safeguarded. However, the District did not accomplish this objective as the District's capital assets and stewardship lists were not accurate and complete with respect to the assets reported, the actual historical cost, useful life, and function in which the asset was being used. Also, equipment items that were recorded on the District's stewardship and capital assets lists were not physically identified by a tag, marked with an identifying number, or specifically identified by some other means. Additionally, the District did not perform a physical inventory within the past 3 years and did not update the lists for acquisitions and disposals. Further, the District did not reconcile capitalized acquisitions to capital expenditures or the current year's capital assets list to the prior year's list. Lastly, accumulated depreciation and depreciation expenditures presented in the financial statements were estimated, rather than calculated using acceptable depreciation methods.

Recommendations

The following procedures can help the District improve its controls over capital assets and ensure that the capital assets and stewardship lists are complete and accurate:

- Prepare and maintain a current capital assets list that includes all equipment with unit costs of \$5,000 or more and useful lives of 1 year or more, and all land, buildings, and related improvements with costs of \$5,000 or more. Include all required information for each item on the list.
- Prepare and maintain a current stewardship list that includes all equipment and vehicles costing between \$1,000 and \$5,000. Include all required information for each item on the list.
- Tag each item on the stewardship and capital assets lists with an identifying number.
- Perform a physical inventory of capital assets every 3 years by an employee independent of any custodial function, and reconcile the results of the inventory with the capital assets and stewardship lists.

USFR pages VI-E-2 and 3 and USFR Memorandum No. 196 describes the information that should be recorded on the capital assets and stewardship lists.

Instructions for performing a physical inventory of capital assets are listed on USFR pages VI-E-8 and 9.

- Continually update the capital assets and stewardship lists or prepare a separate current year capital additions and disposals list during the year to help ensure that items are appropriately added to or deleted from the capital assets and stewardship lists.
- Reconcile capital asset additions to capital expenditures and the current year's capital assets list to the previous year's list. Investigate and resolve all differences.
- Maintain information required for depreciation in the same format as the capital assets list or include it in a separate depreciation schedule that is cross-referenced to the capital assets list.

The forms on USFR pages VI-E-13 and 14 may be used to document the reconciliation of capital assets additions to capital expenditures and the current year's capital assets list to the previous year's list.

FINDING 3

The District should ensure the accuracy of its accounting records and improve its financial reporting

The District did not report accurate financial information to the Arizona Department of Education.

The District's Governing Board depends on accurate information to fulfill its oversight responsibility. The District should also report accurate information to the public and agencies from which it receives funding. To achieve this objective, management should ensure that its accounting records, budgets, and annual financial report (AFR) are accurate and complete. However, the District did not fully accomplish this objective. Specifically, the District did not reconcile its records of revenues, expenditures, and cash balances to the CSS' records, and did not always maintain its accounting records in accordance with the USFR Chart of Accounts. The District also had a negative cash balance in the Fingerprinting Fund. In addition, the District did not maintain a system to account for the accrual and use of compensated leave.

Further, the District's budgeted expenditures reported on the AFR did not agree to the expenditure budget for several funds, and actual expenditures reported on the AFR and food service AFR did not always agree to the District's accounting records. Finally, the approved daily route miles reported on the budget worksheets did not agree to the District's TRAN 55-1 report.

Recommendations

To help ensure the accuracy of its accounting records and improve its financial reporting, the District should:

- Reconcile its cash balances by fund monthly and its records of revenues, expenditures, and cash balances by fund, program, function, and object code, as applicable, to the CSS' records, at least at fiscal year-end. The District should investigate all reconciling items and make any necessary corrections.
- Record all transactions in accordance with the USFR Chart of Accounts.
- Verify that sufficient cash is available in cash-controlled funds before authorizing expenditures.

USFR §III provides guidance for classifying financial transactions.

- Districts should establish and maintain a system to account for the accrual and use of leave for all employees. In addition, the District should retain authorized leave summaries, or other similar forms, to record leave time earned or used for each employee.
- Ensure actual revenues, expenditures, and cash balances agree with the District's accounting records before preparing the AFR and have a second employee verify the amounts before submitting it to ADE.
- Obtain approved daily route miles from the prior year's ADE Transportation Route Report (TRAN 55-1) to complete the expenditure budget worksheets.

FINDING 4

The District's controls over its bank accounts and cash should be strengthened

The District did not safeguard its cash in banks because it did not reconcile its bank accounts.

The District receives cash from various sources, including student activities, and maintains bank accounts to deposit the related receipts. Because of the relatively high risk associated with transactions involving cash, school districts should establish and maintain effective internal controls to safeguard cash. However, the District did not have strong controls over its cash and bank accounts. Specifically, the District did not perform any bank reconciliations for its bank accounts. In addition, the District did not maintain a list of student activities cash balances by club, and the total cash balance on its ledger did not agree to the check register balance.

Recommendations

To strengthen controls over district and student monies, the District should prepare monthly bank reconciliations for all bank accounts in a timely manner. The reconciliations should be prepared by an employee not responsible for handling cash or issuing checks. If this is not possible because of limited staff, the reconciliations should be reviewed by district management and signed and dated by the preparer and the reviewer. Further, the District should ensure its student activities cash balances are recorded by club and that the total of the cash balances agrees to the student activities check register.

Bank account reconciliation procedures are outlined on USFR page VI-C-6.